

CHAPTER 11

AUDITS

- I. **INTRODUCTION.** This chapter details the process for having your program records audited, in accordance with the contract requirements (see Chapter 1 and 2 for contract audit requirements). **Please note that copies of required annual audits do not need to be submitted directly to the state CDBG program but are submitted to the State Controller's Office for review and approval. The Department also reviews and approves the audit and notifies CDBG of annual audit results.**
- II. **GRANTEE RESPONSIBILITIES.** As a grantee of federal funds, you must comply with federal audit requirements. This section covers what is required and when, and outlines how you should prepare for and respond to an audit. **Please note that grantees are also responsible for obtaining audits from subrecipients or other agencies who use CDBG funds to operate programs or projects and you must confirm that the reporting agency is in compliance with OMB Circular A-133.**

The topics covered in this section are:

- A. Audit requirements
 - 1. Definitions
 - 2. Requirements
- B. Preparing for an audit
 - 1. Scheduling audits
 - 2. Selecting an auditor
 - 3. Assembling records
 - 4. Exit interview
 - 5. Audit submittal
 - 6. Payment of audit costs

- C. Resolving audit findings

A. **Audit requirements.**

- 1. Definitions.

Non-federal entity means a State, local government, or non-profit organization.

Federal award means federal financial assistance and federal cost-reimbursement contracts that non-federal entities receive directly from federal awarding agencies or indirectly from pass-through entities. It does not include procurement contracts, under grants or contracts, used to buy goods or services from vendors. Any audits of such vendors shall be covered by the terms and conditions of the contract.

2. Requirements. Pursuant to the Office of Management and Budget (OMB) Circular A-133, non-Federal entities that expend less than \$500,000 in Federal awards (beginning January 1, 2004) are exempt from Federal audit requirements for that year, except as noted in §____.215(a). However, other State or contract audit requirements might apply. A letter to the State Controller's Office (SCO) declaring an exemption from Federal audit requirements is required. There is no form from SCO for this purpose. (See Audit submittal below for address).

Non-Federal entities that expend \$500,000 or more in a year in Federal awards shall have a single audit conducted in accordance with §____.500. If the Federal awards are expended under only one Federal program and the Federal program's laws, regulations, or grant agreements do not require a financial statement audit of the auditee, the auditee may elect to have a program-specific audit conducted in accordance with §____.235.

Your auditor must follow the applicable OMB Circular to complete the audit. (See other references in Section V.)

If you have loaned or granted any of your CDBG funds to a nonprofit organization (e.g., to operate an emergency shelter) then you are responsible for ensuring that the nonprofit agency is in compliance with OMB Circular A-133. This includes monitoring the agency and ensuring that it submits to you a single audit, and monitoring the resolution of any audit findings.

If you have loaned or granted any of your CDBG funds to another jurisdiction, you must ensure that it complies with OMB Circular A-133. This includes monitoring the other agency's use of the funds, receiving a single audit from them, and monitoring the resolution of any audit findings.

- B. Preparing for an audit.** This explains the basic process to prepare for an audit when one is required.

1. Scheduling audits. When an audit is required, the auditee must submit a data collection form and a reporting package in accordance with §____.320(b) and (c). The reports shall be submitted within the earlier of 30 days after receipt of the auditor's report(s) or nine months after the end

of the audit period. For fiscal years beginning on or before June 30, 1998, the audit shall be completed and the data collection form and reporting package shall be submitted within the earlier of 30 days after receipt of the auditor's report(s) or 13 months after the end of the audit period.

2. Selecting an auditor. The selection of an outside Certified Public Accounting (CPA) firm must be consistent with procurement standards prescribed by Attachment O of OMB Circular A-102.

The American Institute of Certified Public Accountants (AICPA) requires that a financial audit be completed by an independent auditor. The audit should not be completed by anyone on the jurisdiction's staff or governing body as this would impair the auditor's independence and call into question the requirement for independence.

3. Assembling records. Prior to the arrival of the auditor, assemble the following CDBG records and files:

- Financial reports submitted to the Department and those received from subgrantees;
- All audit reports issued in the past two years;
- The CDBG contract;
- Copies of the CDBG State Regulations, OMB Circular A-87, GAO's Guidelines for Financial and Compliance Audits of Federally Assisted Programs and this Grant Management Manual;
- All major contracts, such as leases, employment agreements, and major purchase commitments entered into by the organization;
- Cost allocation plan and SCO-approved indirect cost rate plan, if applicable; and
- Source documents, books of original entry and final entry, and worksheets.

4. Exit interview. At the completion of the audit, the auditor should hold an exit conference. At the exit conference, the auditor will present the preliminary opinions and findings (both negative and positive). The jurisdictions should prepare a written response indicating agreement or disagreement to each finding. The response should include the jurisdictions plans to resolve the findings or reasons for disagreement. The auditor will respond to the jurisdictions response in the audit.

5. Audit submittal. Submit the completed audit to the State Controller's Office at:
State Controller's Office
Division of Audits
Financial Audits Bureau/Single Audits Unit
P.O. Box 942850
Sacramento, CA 94250-5874

The SCO will review it and notify the jurisdiction and the Department of any technical compliance issues.

6. Payment of audit costs. Pursuant to OMB Circular A-133 and A-87, the percentage of costs charged to federal assistance programs for a single audit shall not exceed the percentage of CDBG funds expended for the audit period to the jurisdiction's total expenditures being audited. This percentage may only be exceeded if appropriate documentation demonstrates higher actual costs.

Please refer to §____.230 for audit costs that cannot be charged to CDBG grants.

- C. **Resolving audit findings.** If there are audit findings, a detailed response explaining the action(s) taken to resolve the finding must be submitted to the Department within 6 months of the audit report date. The Department will review the response and, if in agreement, will notify the jurisdiction in writing that the finding has been resolved. If the Department is not in agreement with the resolution, it will advise the jurisdiction in writing the corrective actions(s) required to resolve the finding. This action could include the repayment of disallowed costs. Timely resolution of audit findings is very important because it could jeopardize your current and future CDBG funding.

III. **COMMON PROBLEMS.**

- Books not maintained on a current basis or not kept in accordance with standards contained in the State regulations
- All receipts, (e.g., CDBG advances, loan application fees, rental income, program fees, bid deposits, etc.) not recorded
- Bank reconciliation's and subsidiary ledgers not maintained (such as rehabilitation loan ledgers that accurately identify amounts borrowed, payments, additions and balances)
- Financial data, as shown on performance reports, does not agree with the books

- Unsupported or insufficient support for payments
- Expenditures made prior to the date the Department signed the grant agreement
- Program income not used for approved CDBG activities
- Funding of projects outside approved geographic boundaries described in the application

IV. DEPARTMENT'S/STATE'S ROLE. Once the audit is completed, counties and cities must submit the annual audit to the State Controller's Office . SCO will then review the audit for technical accuracy, and will notify you and the Department if the audit meets the financial and compliance audit requirements of generally accepted governmental auditing standards.

If SCO determines there are unresolved compliance issues the Department will be advised and directed to resolve the issues with the grantee.

V. REFERENCES.

- State CDBG Regulations, Section 7122, contains the audit requirements for the State CDBG Program.
- Government Auditing Standards (Yellow Book) published by the U.S. General Accounting Office contains audit standards for the audit of organizations receiving federal funds for their programs, activities, functions, and for federal funds received by contractors, nonprofit organizations, and other external organizations.
- OMB Circular A-87 establishes principles and standards for determining costs applicable to grants, contracts, and other agreements with State and local governments.
- OMB Circular A-102, Grants and Cooperative Agreements with State and Local Governments describes the auditing requirements for local jurisdictions.
- OMB Circular A-133 requires that the audit of State, local governmental, and non-profit organizations, programs, activities, and functions performed by State or local government auditors or by public accountants be made in accordance with General Accounting Office audit standards. *A copy of OMB Circular A-133 may be obtained on the internet at www.whitehouse.gov/omb/circulars/a133/a133.html.*
- Compliance Guidelines for Audits of Subrecipients of Federal Financial Assistance contains instructions for the State implementation of OMB Circular A-128.
- Public Law 98-502 - the Single Audit Act of 1984

VI. SUPPORTING MATERIALS.

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